Our performance: 2010 financial overview

In 2010, Pearson's sales increased by 10% in headline terms to £5.7bn and adjusted operating profit by 21% to £857m. The headline growth rates include a benefit from currency movements and acquisitions. Currency movements added £128m to sales and £39m to operating profit. This was the result of the strengthening of the US dollar and other currencies against sterling: we generated approximately 60% of our sales and profits in US dollars and the average exchange rate strengthened from £1:$1.57 in 2009 to £1:$1.54 in 2010. At constant exchange rates (ie stripping out the benefit of those currency movements), our sales and operating profit grew 8% and 15% respectively.

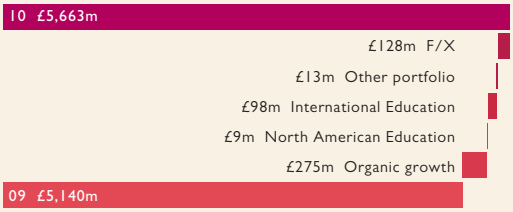
Acquisitions, primarily in our education company, contributed £120m to sales and £5m to operating profits. This includes integration costs and investments related to our newly-acquired companies, which we expense.

Our underlying revenue and operating profit (ie stripping out the benefit of both portfolio changes and currency movements) grew 5% and 14% respectively.

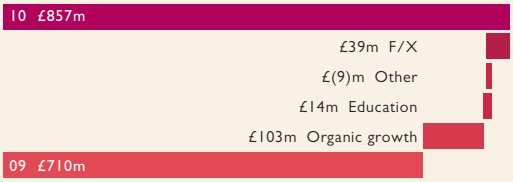
The disposal of Interactive Data was completed on 29 July 2010. Interactive Data therefore contributed seven months of profit in 2010, compared to a full twelve months in 2009. Pearson's total operating profit increased 9% in headline terms to £938m, reflecting this part-year contribution from Interactive Data in 2010.

Our tax rate in 2010 was 25.2%, a little lower than in 2009. We increased adjusted earnings per share by 19% in headline terms to 77.5p.

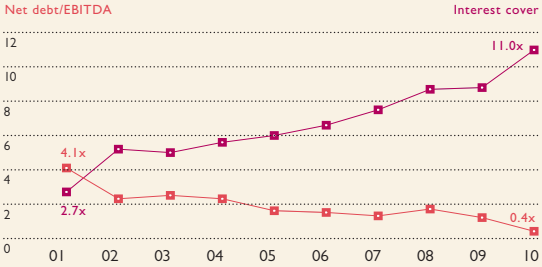
SALES GROWTH £m +8%



PROFIT GROWTH £m +15%



BALANCE SHEET STRENGTH



AVERAGE WORKING CAPITAL/SALES %

Our performance: 2010 financial overview continued

Cash generation

We increased operating cash flow by £144m to £1,057m (headline growth of 16%) and free cash flow by £181m to £904m, or 112.8p per share (headline growth of 25%). We converted 113% of operating profit into cash, with our average working capital: sales ratio improving by a further five percentage points to 20.1% as we benefited from the rapid growth in our digital businesses and continued efficiency improvements.

Return on invested capital

We improved our return on average invested capital by 1.4 percentage points to 10.3%, benefiting from strong profit growth and tight control of working capital as well as the part year contribution from Interactive Data.

Statutory results

Our statutory results show an increase of £124m in operating profit to £743m (£619m in 2009). Basic earnings per share were 161.9p in 2010, up from 53.2p in 2009, helped by the profit on disposal of Interactive Data.

Balance sheet

We significantly reduced our net debt by £662m to £430m (£1,092m in 2009). We benefited from the proceeds from the sale of Interactive Data and strong cash generation, partly offset by acquisition investment of £535m and sustained investment in our businesses. Since 2000, Pearson's net debt/EBITDA ratio has fallen from 3.9x to 0.4x and our interest cover has increased from 3.1x to 11.0x.

Dividend

The board is proposing a dividend increase of 9% to 38.7p, subject to shareholder approval. 2010 will be Pearson's 19th straight year of increasing our dividend above the rate of inflation and our fastest rate of growth in a decade. Over the past ten years we have increased our dividend at a compound annual rate of 6%, returning more than £2.3bn to shareholders. We have a progressive dividend policy of sustaining our dividend cover at around 2.0x over the long term while moving our dividend growth more in line with earnings growth.

Outlook: 2011

Over the past five years Pearson has produced, on average, 16% growth in earnings and cash flow. We sustained our growth even in the face of very tough economic and market conditions in recent years. We are planning for some of our markets to remain weak in 2011, particularly those that depend on government spending and traditional print publishing business models. In addition, we face tough comparatives (especially in the first half of the year) after our particularly strong competitive and financial performance in 2010.

Even so, we have built a series of competitive advantages which should help us deliver another good year in 2011. These advantages include our sustained investment, digital leadership, educational effectiveness, positions in fast-growing economies and operating efficiency.

Education

In education, we expect to achieve continued growth in 2011. In North America, we see growth in higher education (despite slower enrolment rates) and assessment more than offsetting a slower year for the school publishing industry (the result of the lower new adoption opportunity and pressure on state budgets). Our International education business will benefit from its rapidly-growing position in services, technology and developing economies, enabling it to grow again despite the weak public spending environment in some markets.

FT Group

At the FT Group, we are rapidly shifting our business model towards digital and subscription revenues. Advertising revenues remain unpredictable, but we see healthy demand for the FT's premium content, especially in digital formats, and a recovery in business conditions for Mergermarket.

Penguin

Penguin will face another year of fast-changing industry conditions, driven by the rapid growth of both digital sales channels and digital books, and by the resulting pressures on physical bookstores. After particularly strong competitive performance and financial results in 2010, we expect Penguin to perform in line with the overall consumer publishing industry this year, while we continue to adapt the business to these industry changes.

Interest and tax

In 2011, our lower net debt level and pension finance charge will result in a lower interest charge to adjusted earnings than in 2010. We expect our P&L tax charge against adjusted earnings to be in the 24–26% range and our cash tax rate to be in the 15–20% range.

Exchange rates

Pearson generates approximately 60% of its sales in the US. A five cent move in the average £:$ exchange rate for the full year (which in 2010 was £1:$1.54) has an impact of approximately 1.3p on adjusted earnings per share.

North American Education

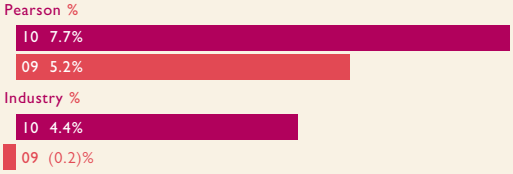
North American Education is Pearson's largest business, with 2010 sales of £2.6bn and operating profit of £469m.

Building on our roots as a leading publisher of educational materials and provider of assessment services, we have made significant investments and change to transform Pearson into a world-leading provider of learning technologies for students and enterprise technologies for educational institutions. These technology services – including eCollege, PowerSchool, the MyLabs and Edustructures – are the backbone of our strategy to help educators raise student performance and institutions to become more effective.

KEY PERFORMANCE INDICATORS

£ millions	2010	2009	Headline growth	CER growth	Underlying growth
Sales	2,640	2,470	7%	5%	4%
Adjusted operating profit	469	403	16%	14%	12%

US EDUCATION PUBLISHING SCHOOL AND COLLEGE SALES GROWTH VS INDUSTRY



Pearson's total year-on-year sales growth in school and college education publishing products in the US versus the year-on-year sales growth of the total US industry.

SCHOOL PUBLISHING ADOPTION CYCLE WIN RATES

Pearson's market share by value of new business in the US adoption states. Market share is quoted as a percentage of the total value of adoptions that we participated in.

ASSESSMENT AND INFORMATION TESTING CONTRACT WIN RATES

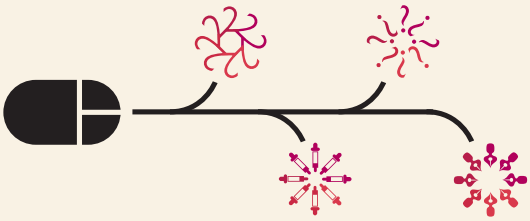
The lifetime value of US testing contracts won by Pearson this year as a percentage of the total lifetime value of competitive contracts bid for this year.

ONLINE LEARNING USERS

The number of registrations by students to access one of our US online learning programmes.

Higher Education highlights in 2010 include:

- The US Higher Education publishing market grew 7.3% in 2010, according to the Association of American Publishers, with the industry seeing healthy enrolment growth and good demand for instructional materials. Pearson gained share, benefiting from its lead in technology and customisation, and has now grown faster than the US higher education industry for 12 consecutive years.



- Pearson's pioneering 'MyLab' digital learning, homework and assessment programmes grew strongly with student registrations up 32% to more than 7.3 million. Evaluation studies show that the use of MyLab programmes can significantly improve student test scores and institutional efficiency http://bit.ly/fWPic0
- We launched LearningStudio, a broad suite of learning management technologies including eCollege and Fronter. We increased fully-online student enrolments by 54% to 8.3 million in North America. Renewal rates remain high at approximately 90% by value.

Assessment and Information highlights in 2010 include:

- Revenues at our Assessment and Information division were broadly level with 2009. State funding pressures made market conditions tough for our state assessment and teacher testing businesses; these were offset by good growth in diagnostic and clinical assessments. Assessment and Information achieved good profit growth, benefiting from a shift to premium products and further efficiencies generated from the integration of the Harcourt Assessment business.

AMERICA'S CHOICE

Partners in education

We acquired America's Choice to boost Pearson's services in school reform, a major focus of the US education department. America's Choice brings together instruction, assessment, leadership development, professional development, coaching and ongoing consulting services.

To learn more about America's Choice, watch our film at www.pearson.com/films

North American Education continued

- We renewed two important contracts, extending our long-standing relationships with the College Board to administer the SATs and with the Texas Education Agency to administer state-wide student assessments.
- We continue to achieve strong growth in secure online testing, delivering 13.3 million online tests in 2010, up 41% over 2009.
- Our market-leading student information systems business in the US continued to achieve rapid organic growth further boosted by the acquisition of Administrative Assistants Limited in 2010. We now support almost 16 million US students, an increase of 49% over 2009.
- We achieved strong growth with AIMSWEB, our progress monitoring service which enables early intervention and remediation for struggling students. AIMSWEB now supports almost four million students, an increase of more than 20%.

School Curriculum highlights in 2010 include:

- The US School publishing market grew 3.2% in 2010, according to the Association of American Publishers. State budgets continue to be under pressure but the industry returned to growth, benefiting from the stronger new adoption opportunity this year (total opportunity of $800m in 2010 against $500m in 2009).
- Pearson gained share with a strong performance from enVisionMATH, Pearson's pioneering digital math curriculum. A two-year study in elementary schools concluded that students using enVisionMath demonstrated significantly greater improvement in math computation, math problem-solving and math communication compared to students using other math programs. In computation they jumped the equivalent of five grade levels in two years.

- Successnet, our online learning platform for teachers and students which supports Pearson's digital instruction, assessment and remediation programmes, grew strongly. It generated almost six million registrations in 2010, up 33% on 2009, with the number of assessments taken through the system increasing 53% to more than eight million.

› We continue to develop digital programmes, platforms and mobile apps to boost achievement and to increase access and affordability. We successfully launched three major new school programmes:

digits (right)

Writing Coach www.phwritingcoach.com a blended print and online programme that helps middle and high school students in writing and grammar with personalised assignments and grading. Studies of classes using the technology behind Writing Coach show significant gains in writing proficiency as measured by district and state assessments;

Online Learning Exchange, an open education resource that allows teachers to create personalised digital learning programmes using standards-based Pearson content as well as teacher-generated material.

› Poptropica www.poptropica.com is the largest virtual world for young children in the US with average monthly unique visitors growing by 40% to 8.1 million from more than 100 countries and speaking more than 70 languages. Poptropica launched seven new islands and was the fifth most searched-for video game on Google.com in 2010.

DIGITS

Twice as much time for teaching

digits, our digital middle school maths programme, provides powerful services for teachers including embedded assessment, differentation of students and automation of administrative tasks. In field tests and pilots, digits helped to make teachers more efficient, doubling the amount of time they had to devote to instruction. http://bit.ly/i9NcId

International Education

Our International Education company, the world leader by revenues, is active in more than 70 countries.

It is a major focus of our strategy, and sales and profits have doubled since 2006. Our strategy is to combine educational content, assessment, technologies and related services to help educational institutions become more effective and their students more successful. We expect to benefit from a series of powerful long-term global trends: increasing public and private spending on education (despite current pressures on public spending in developed markets); growing participation rates in elementary, secondary and higher education; the demand for assessment to provide measures of achievement; the growing technology infrastructure in educational institutions; and the rise of English as a global language.

Our International Education business has significant exposure to a wide range of currencies including the US dollar and the euro. In 2010, currency movements boosted revenues by £38m and adjusted operating profits by £15m compared to 2009.

KEY PERFORMANCE INDICATORS

£ millions	2010	2009	Headline growth	CER growth	Underlying growth
Sales	1,234	1,035	19%	16%	6%
Adjusted operating profit	171	141	21%	10%	8%

ONLINE LEARNING USERS

MyLab Registrations no.

The number of registrations by students and professors to access one of our International Education online learning programmes.

ONLINE RESULTS LOGINS

Logins no.

Number of logins by users of International Education's online results service.

Global highlights in 2010 include:

- We acquired Wall Street Institute (WSI), which provides premium spoken English training for adults, for $101m in cash. WSI has about 340 franchised learning centres in 25 territories in Asia, Europe, the Middle East and Africa.
- More than 670,000 students used our MyLab digital learning, homework and assessment programmes, an increase of more than 40%. They included 150,000 users of our online English-language products MyEnglishLabs and MyNorthStarLab, a 170% increase.
- Our eCollege learning management system won new contracts in Malaysia and Colombia. Our Fronter learning management system continued to grow strongly with unique registration rising more than 20% to 1.1 million students in more than 8,700 schools, colleges and universities around the world.

› Pearson Learning Solutions, which combines products and services from across Pearson to deliver a systematic approach to improving student performance, won new contracts in South Africa, Malta, Vietnam and the UK.

UK highlights in 2010 include:

› BTEC, our flagship vocational qualification, attracted more than 1.4 million student registrations, up 28% on 2009. Research suggests that a BTEC National qualification can increase an individual's lifetime earnings by up to £92,000. Registrations for our NVQ work-based learning qualification grew 45% to more than 165,000, and we introduced the BTEC Apprenticeship to serve the work-based learning market.

› We marked more than 5.4 million A/AS Level and GCSE and Diploma scripts in the 2009–2010 academic year, with 90% now marked on screen. Pearson marked and delivered 3.4 million tests in six weeks for the National Curriculum Tests at Key Stage 2.

› Pearson announced plans to create a vocational degree, to boost student access to higher education in the UK and around the world. The first phase of degree programmes will be developed in business, engineering, IT and health and social care.

› We established a new school improvement business in the UK, which will work with schools to help them train teachers, improve strategic planning and structure teaching methods.

Continental Europe highlights in 2010 include:

› In Italy, adoption of our Linx digital secondary science programme increased three-fold, helping Pearson to grow strongly and become joint market leader for combined lower and upper secondary education. Linx is built around content from our North American science programmes customised for the Italian market. We began to develop a broader range and depth of digital products and services, including teacher training, to personalise learning and increase educational effectiveness.

› In the Netherlands, we launched iPockets, the first fully digital Early English course for 4-8 year-olds in primary education. The course is 100% digital and subscription based and customised for the Dutch market.

WALL STREET ENGLISH

Starting a global conversation

Student enrolments at our Wall Street English schools increased by 27%. We announced plans to open 50 new English language centres in China adding to the 66 centres and schools already operating under the Wall Street English and Longman English brands. We also acquired Wall Street Institute (WSI), which provides premium spoken English training for adults, for $101m in cash. WSI has about 340 franchised learning centres in 25 territories in Asia, Europe, the Middle East and Africa.

To learn more about Wall Street English, watch our film at www.pearson.com/films

International Education continued

Africa and the Middle East highlights in 2010 include:

- In South Africa's Western Cape province, we won a three-year contract to prepare, administer and report all Grade 9 student assessments. The tests focus on both individual student results and the systemic performance of schools and districts.
- Pearson won new national contracts in Ethiopia, to supply 2.9m Biology and Physics learning materials for Senior Secondary Grades 9 to 12. In Zimbabwe, we were awarded a contract by UNICEF to deliver 13.5 million textbooks to children in Grades 1–7 in mathematics, environmental science, English, Shona and Ndebele.

- Pearson announced its intention to acquire a 75% stake in CTI Education Group of South Africa, one of South Africa's leading private higher education institutions, for £31 million in cash. CTI serves more than 9,000 students on 12 campuses.

To learn more about CTI Education Group, watch our film at www.pearson.com/films

- We generated strong growth in the Gulf region in higher education with integrated technology products in Business & Economics and Science.

Asia highlights in 2010 include:

- Wall Street English (see previous page).
- In January 2011, Pearson agreed to increase its shareholding in Indian education company TutorVista to a controlling 76% stake for a consideration of $127m. TutorVista supplies digital content and technology platforms, online tutoring and services to K-12 schools.

To learn more about TutorVista, watch our film at www.pearson.com/films

Latin America highlights in 2010 include:

- Our School curriculum business grew strongly, particularly in Mexico, Colombia, Chile and Peru, as we continued to build our locally developed materials as well as Spanish language adaptations of US school programmes.
- Strong growth of English Language Teaching materials across Latin America underpinned by performance in Brazil, Colombia, Argentina, Chile, Dominican Republic and Peru.

SISTEMA EDUCACIONAL BRASILEIRO

Learning: a systemic approach

Pearson agreed a strategic partnership with Sistema Educacional Brasileiro (SEB) in Brazil to provide services to its educational institutions and to acquire its school learning systems ('sistema') business for $517m. SEB's serves more than 450,000 students across both private and public schools.

To learn more about SEB, watch our film at www.pearson.com/films

Professional Education

Our Professional business is focused on publishing, training, testing and certification for professionals.

Over the past five years, we have increased operating profit from £17m in 2006 to £51m in 2010. We expect these businesses to benefit from rising demand for work-related skills and qualifications in both developed and developing markets and from close connections with professional content and customers in other parts of Pearson.

Professional testing highlights in 2010 include:

- We continued to see good growth at Pearson VUE, with test volumes up 3% on 2009 to approximately 8 million. Average revenues per test are increasing as we develop a broader range of services and enhance our systems and assessments to meet our customers' current and future needs.
- Pearson VUE renewed a number of major contracts including the Driving Standards Agency (DSA) of Great Britain and the Driver & Vehicle Agency (DVA) of Northern Ireland; Cisco; and Colorado Department of Regulatory Agencies. On 11 January 2011, we announced a 12-year extension of our relationship with the Graduate Management Admission Council to administer the Graduate Management Admission Test.
- We also won a number of new contracts to deliver computer-based tests in the US, UK and the Middle East, covering the real estate, accountancy, legal, healthcare, skills and finance sectors.

Professional publishing highlights in 2010 include:

- Our Professional publishing business was level in 2010 with steady margins as strong growth in digital products and services offset continued challenging trading conditions in the retail market and international markets, as well as a planned reduction in the number of print titles published.

KEY PERFORMANCE INDICATORS

£ millions	2010	2009	Headline growth	CER growth	Underlying growth
Sales	333	275	21%	20%	6%
Adjusted operating profit	51	43	19%	16%	5%

- We launched online learning products with customisable content, assessment and personalised study paths and also delivered 450 hours of technical training through online subscriptions for the IT certification market.
- We developed applications for social networks and mobile devices to extend the reach and accessibility of our content and videos available within our Safari Books Online platform.

Professional training highlights in 2010 include:

- We acquired Melorio plc, one of the UK's leading vocational training groups, for £98m, supporting our vocational education strategy by combining Melorio's training delivery skills with our existing complementary strengths in educational publishing, technology and assessments. Melorio traded well in the second half of the year securing a number of large key contracts for training delivery, and successfully graduating and placing the largest IT graduate cohort in the history of the business. Our investment in systems, streamlining the course offering and training centres and back office integration are all on track.

To learn more about Melorio, watch our film at www.pearson.com/films

GMAT RETAINED

A testing decade

At the start of 2011, our largest professional testing contract with the Graduate Management Admission Council to administer the GMAT test was renewed until 2022.

Business Information: FT Group

The FT Group is a leading provider of essential information in attractive niches of the global business information market.

These include insight, news and analysis and indices provided through a growing number of print, digital and mobile channels. In recent years, The FT Group has significantly shifted its business towards digital, subscription and content revenues and has continued to invest in talent and in services in faster growing emerging markets. In 2010, digital services accounted for 40% of FT Group revenues, up from 14% in 2006. Content revenues comprised 55% of total revenues, up from 33% in 2006, while advertising accounted for 45% of FT Group revenues, down from 67% in 2006.

KEY PERFORMANCE INDICATORS

£ millions	2010	2009	Headline growth	CER growth	Underlying growth
Sales	403	358	13%	12%	9%
Adjusted operating profit	60	39	54%	54%	49%

FT CIRCULATION REVENUE GROWTH

The FT newspaper's year-on-year growth in circulation revenue.

FT.COM AVERAGE MONTHLY UNIQUE USERS FOR THE YEAR

The average monthly number of unique users of FT.com for the year.

MERGERMARKET RENEWAL RATES

The current year value of sales to existing customers as a percentage of their spend in the previous year.

Financial Times highlights in 2010 include:

- The FT's combined paid print and digital circulation reached 597,000 in the fourth quarter of 2010.
- After weak advertising markets in 2009, we saw good advertising growth in 2010 although the visibility for advertising revenues is poor.
- We extended the breadth and depth of the FT's premium subscription services through the launch of FT Tilt, focused on emerging markets; the launch of MandateWire US, extending the reach of this successful European brand into new markets; and the acquisition of Medley Global Advisors, a premier provider of macro policy intelligence.

To learn more about Medley Global Advisors, watch our film at www.pearson.com/films

Mergermarket highlights in 2010 include:

› The Mergermarket Group benefited from improving market conditions and its flexibility in adapting to new client investment strategies, which supported stronger renewal rates and new business revenues. An increase in global M&A activity benefited mergermarket and dealReporter; continued volatility in debt markets helped sustain the strong performance of DebtWire.

› Strong growth in developing markets supported by new product launches including our first local language version of mergermarket in China.

› In March 2010 we acquired Xtract research, which provides bond covenant data to help investors understand the impact of covenants on valuation.

Joint ventures highlights in 2010 include:

› *The Economist,* in which Pearson owns a 50% stake, increased global weekly circulation by 3.7% to 1.47 million (for the July–December 2010 ABC period); total annual online visits increased to 118 million, up 21% on 2009.

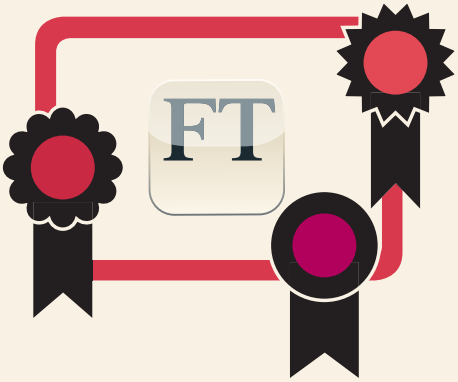
› **FTSE,** our 50%-owned joint venture with the London Stock Exchange, increased revenues by 20% and acquired the remaining 50% of FXI, FTSE's JV with Xinhua Finance in China.

› **Business Day and Financial Mail (BDFM),** our 50% owned joint-venture in South Africa with Avusa, returned to profitability with revenue increasing by 5%. The business benefited from a recovery in advertising and the closure of non-profitable operations.

FT ONLINE

Award-winning app, Award-winning content

The FT provided strong and accelerating growth in its digital readership with digital subscriptions up over 50% to 207,000, more than 1,000 direct corporate customers and registered users up 79% to more than three million. It generated over 900,000 downloads of FT apps on mobile phones and tablet devices and scooped a prestigious Apple Design Award for its iPad app.



Consumer Publishing: Penguin

Penguin is one of the most famous brands in book publishing, known around the world for the quality of its publishing and its consistent record of innovation.

Over the past five years, Penguin's profits have increased at an annual average rate of 8%.

In 2010 Penguin achieved record sales and profits in a challenging and rapidly-changing industry environment. Penguin's profits were struck after making additional provisions for a number of credit exposures in the book retailing sector, including in relation to Borders in the US. Our market share gains and improved profitability were the result of three factors in particular:

1. An outstanding US publishing performance included a record number of bestsellers, an increase in market share and rapid expansion in emerging digital platforms and formats;

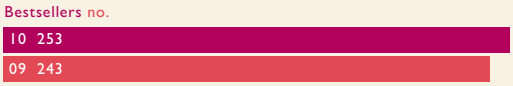
2. Penguin in the UK celebrated the best year in its history, leading the bestseller lists and increasing its market share by 2 percentage points to 10%;

3. DK captured the benefits of its 2009 reorganisation, with sales of Lego Star Wars titles boosting revenue and the transfer of cost centres to India enhancing its margin.

KEY PERFORMANCE INDICATORS

£ millions	2010	2009	Headline growth	CER growth	Underlying growth
Sales	1,053	1,002	5%	2%	6%
Adjusted operating profit	106	84	26%	10%	26%

US BESTSELLERS



The number of Penguin books entering the Top Ten bestseller lists in the US (New York Times).

UK BESTSELLERS

The number of Penguin books entering the Top Ten bestseller lists in the UK (Nielsen BookScan Top Ten).

E-BOOK SALES

Penguin global e-book sales as a percentage of Penguin Group net sales.

Global highlights in 2010 include:

- A strong and consistent publishing performance across imprints and territories produced market share gains in the US, UK and Australia, our three largest markets.
- Strong growth in developing markets was boosted by the launch of new imprints and the increasing breadth and depth of our local publishing programmes in India, China and South Africa.
- Continued investment in global publishing with the launch of Penguin's Classics in Portuguese and Arabic, joining existing Mandarin and Korean editions; the launch in India of a new imprint in partnership with bestselling author and superstar Shobhaa De; and the continued international roll-out of our non-fiction imprint Allen Lane in Canada.

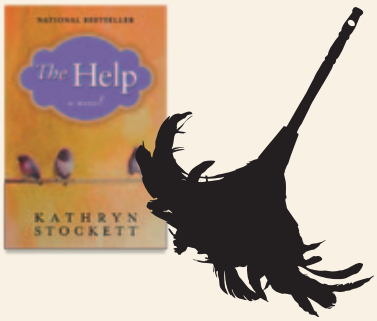
Digital highlights in 2010 include:

- eBook sales were up 182% on the previous year and now account for 6% of Penguin revenues worldwide.
- We accelerated our investment in digital products and innovation with new app releases in the children's market including Spot, Peppa Pig, The Little Engine That Could, Ladybird's Babytouch and the Mad Libs app, which was named one of the best apps at the 2010 E-Book Summit. For adults, we launched the groundbreaking myFry app, published the amplified ebook of Ken Follett's international bestselling novel *The Pillars of the Earth*, featuring video, art and music from the original TV series; and we introduced ten DK Eyewitness Top Ten Travel Guides apps with more to follow in 2011.
- Penguin continued to invest to transform its internal publishing processes onto Pearson-wide digital platforms, enabling faster product development and more efficient creation and re-use of content.

Publishing performance highlights in 2010 include:

- Penguin performed strongly in the US with a broad range of number one bestsellers from repeat authors such as Charlaine Harris, Nora Roberts, Tom Clancy, Ken Follett and Patricia Cornwell.

- Kathryn Stockett's *The Help* stayed on the *New York Times* bestseller list for the whole of 2010 and has sold more than three million copies to date.



JAMIE OLIVER

The UK's biggest selling non-fiction title of the last decade

Jamie Oliver's *30 Minute Meals* sold 1.2 million copies to become the UK's biggest selling hardback non-fiction title of the last decade.

Consumer Publishing: Penguin continued

Publishing performance highlights continued:

- Our outstanding performance in the UK, resulting in our market share rising two percentage points to 10%, was led by Jamie Oliver's *30 Minute Meals*. It sold 1.2 million copies to become the UK's biggest selling non-fiction title of the last decade. Major bestsellers included Stephen Fry's *The Fry Chronicles*, Kathryn Stockett's *The Help*, and *The History of the World in 100 Objects* (published in partnership with the BBC and the British Museum), as well as the Percy Jackson and *Diary of a Wimpy Kid* series.
- DK produced a very good year thanks in part to its top-performing franchise LEGO (*Lego Star Wars Visual Dictionary* was on the *New York Times* bestseller list for the whole of 2010 with 18 weeks at number one). Other bestselling titles included *The Masterchef Cookbook, Complete Human Body* and *Natural History*. DK continues to benefit from the organisation changes made in 2009 as well as the ongoing development of its publishing centre in India.
- Penguin Children's had an excellent year in the US, with Penguin Young Readers Group achieving a record 39 *New York Times* bestsellers, and in the UK, where we reclaimed our position as the number one children's publisher with significant market share gains.
- In 2011, we will publish books from some of our leading authors including, in the US, Patricia Cornwell, Sue Grafton, Charlaine Harris, Nora Roberts, Henry Kissinger, Betty White, Richelle Mead, John Grisham and Eric Carle; and, in the UK, Jamie Oliver, Stephen Fry, Rob Brydon, Jeff Kinney, Rick Riordan and David Almond.

THE FRY CHRONICLES

Number one in five categories

Stephen Fry's *The Fry Chronicles* made publishing history as the first title to hit number one in five categories: hardback, eBook, enhanced eBook with videos featuring the author, audio book and an innovative app that allows readers to delve in and out of the book by topic.

Other financial information

Net finance costs

£ millions	2010	2009
Net interest payable	(73)	(86)
Finance costs in respect of retirement benefit plans	(12)	(12)
Net finance costs reflected in adjusted earnings	(85)	(98)
Other net finance income	12	2
Total net finance costs	(73)	(96)

Net finance costs reported in our adjusted earnings comprise net interest payable and net finance costs relating to retirement benefit plans.

After excluding discontinued businesses, net interest payable in 2010 was £73m, down from £86m in 2009. Although our fixed rate policy reduces the impact of changes in market interest rates, we were still able to benefit from a fall in average US dollar and sterling interest rates during the year. Year-on-year, average three month LIBOR (weighted for the Group's net borrowings in US dollars and sterling at each year end) fell by 0.3% to 0.4%. This reduction in floating market interest rates drove the Group's lower interest charge. However, the low rates on deposited funds coupled with the impact on the calculation of significantly lower net debt, created an increase in the Group's average net interest payable of 5.3% to 7.9%. The Group's average net debt fell by £681m, reflecting the impact of the Interactive Data disposal.

Finance charges relating to post-retirement plans were £12m in both 2010 and 2009. Also included in the statutory definition of net finance costs are foreign exchange and other gains and losses. These are excluded from adjusted earnings as they represent short-term fluctuations in market value and are subject to significant volatility. These other gains and losses may not be realised in due course as it is normally the intention to hold the related instruments to maturity. In 2010 the total of these items excluded from adjusted earnings was a profit of £12m compared to a profit of £2m in 2009.

Funding position and liquid resources

The Group finances its operations by a mixture of cash flows from operations, short-term borrowings from banks and commercial paper markets, and longer-term loans from banks and capital markets. Our objective is to secure continuity of funding at a reasonable cost from diverse sources and with varying maturities. The Group does not use off-balance sheet special purpose entities as a source of liquidity or for any other financing purposes.

The net debt position of the Group is set out below.

£ millions	2010	2009
Cash and cash equivalents	1,736	750
Marketable securities	12	63
Net derivative assets	134	103
Bonds	(2,226)	(1,923)
Bank loans and overdrafts	(73)	(70)
Finance leases	(13)	(15)
Net debt	(430)	(1,092)

The main contributor to the change in the Group's net debt is the increase in cash balances due primarily to the Interactive Data disposal in July 2010 and strong cash collection at the end of 2010. Reflecting the geographical and currency split of our business, a large proportion of our debt is denominated in US dollars (see note 19 for our policy). The weakening of sterling against the US dollar during 2010 (from $1.61 to $1.57:£1) slightly increased our reported net debt.

The Group's credit ratings remained unchanged during the year. The long-term ratings are Baa1 from Moody's and BBB+ from Standard & Poor's, and the short-term ratings are P2 and A2 respectively. The Group's policy is to strive to maintain a rating of Baa1/BBB+ over the long term.

In May 2010, the Group accessed the capital markets, raising $350m through the sale of notes maturing in 2016 and bearing interest at 4%. Of the $350m issued, $300m was swapped to floating rate to conform with the policy described in note 19. The proceeds were used to fund the Group's working capital requirements.

Other financial information continued

In November 2010, the Group negotiated a new $1,750m committed revolving credit facility which matures in November 2015. At 31 December 2010 this facility was undrawn. The facility is intended to be used for short-term drawings and providing refinancing capabilities, including acting as a back-up for our US commercial paper programme. This programme is primarily used to finance our US working capital requirements, in particular our US educational businesses which have a peak borrowing requirement in July. At 31 December 2010, no commercial paper was outstanding.

The Group also maintains other committed and uncommitted facilities to finance short-term working capital requirements in the ordinary course of business.

Further details of the Group's approach to the management of financial risks are set out in note 19 to the financial statements.

Taxation

The effective tax rate on adjusted earnings in 2010 was 25.2% which compares to an effective rate of 25.5% for 2009. Our overseas profits, which arise mainly in the US, are largely subject to tax at higher rates than the UK corporation tax rate (which had an effective statutory rate of 28% in 2010 and in 2009). These higher tax rates were offset by amortisation-related tax deductions and the utilisation of previously unrecognised operating tax losses and credits.

The reported tax charge on a statutory basis was £146m (21.8%) compared to a charge of £146m (27.9%) in 2009. The reduction in the statutory rate is largely due to the recognition of tax losses and credits in the year including pre-acquisition and capital losses that were utilised in connection with the Interactive Data sale. The tax charge relating to that sale in July 2010 is included in the loss on discontinued businesses. Tax paid in 2010 was £335m compared to £103m in 2009 and includes £250m relating to the Interactive Data sale.

Discontinued operations

On 29 July 2010, Pearson's 61% share in Interactive Data Corporation was sold to Silver Lake and Warburg Pincus for $2bn. The results of Interactive Data have been included as discontinued operations in these financial statements. Interactive Data's adjusted operating profit for the seven months to the date of sale was £81m compared to a full year contribution in 2009 of £148m. Also included in discontinued operations in 2010 is the gain on sale of Interactive Data of £1,037m and the attributable tax charge of £306m. The total profit from discontinued operations after taking account of the above items, intangible amortisation, interest and related tax was £776m in 2010 compared to £85m in 2009.

Segmental analysis

During the course of 2010, a number of minor changes to management responsibilities in certain countries were made which have affected reported 2010 segmental numbers in Penguin, North American Education and International Education. The amounts concerned have no impact on the Group as a whole and have been treated as portfolio changes in 2010 for the purposes of calculating growth rates. The 2009 figures have not been restated as the amounts are not considered to be significant. The effect of these changes in the 2010 financial statements has been to reduce the sales and profits at Penguin by £41m and £12m respectively, to increase sales and profits at International Education by £52m and £3m respectively and to reduce sales by £11m and increase profits by £9m in the North American Education segment.

Non-controlling interest

The non-controlling interest in the income statement comprises mainly the publicly-held share of Interactive Data for the period to disposal in July 2010. There are also non-controlling interests in the Group's businesses in South Africa, Nigeria, China and India although none of these are material to the Group numbers. The non-controlling interest in the Group's newly acquired Brazilian business, Sistema Educacional Brasileiro (SEB), is expected to be bought out in the first half of 2011.

Other comprehensive income

Included in other comprehensive income are the net exchange differences on translation of foreign operations. The gain on translation of £173m in 2010 compares to a loss in 2009 of £388m and is principally due to movements in the US dollar. A significant proportion of the Group's operations are based in the US and the US dollar weakened in 2009 from an opening rate of £1:$1.44 to a closing rate at the end of that year of £1:$1.61. At the end of 2010 the US dollar had strengthened slightly in comparison to the opening rate moving from £1:$1.61 to £1:$1.57.

Also included in other comprehensive income in 2010 is an actuarial gain of £71m in relation to post retirement plans. This gain largely arises from improved asset returns for the UK Group pension plan and compares to an actuarial loss in 2009 of £302m. The 2009 loss arose as the assumptions relating to inflation, mortality and the discount rate used in the actuarial valuation all contributed to an increase in the value of liabilities.

Dividends

The dividend accounted for in our 2010 financial statements totalling £292m represents the final dividend in respect of 2009 (23.3p) and the interim dividend for 2010 (13.0p). We are proposing a final dividend for 2010 of 25.7p, bringing the total paid and payable in respect of 2010 to 38.7p, a 9.0% increase on 2009. This final 2010 dividend was approved by the board in February 2011, is subject to approval at the forthcoming AGM and will be charged against 2011 profits. For 2010 the dividend is covered 2.0 times by adjusted earnings.

We seek to maintain a balance between the requirements of our shareholders for a rising stream of dividend income and the reinvestment opportunities which we identify around the Group and through acquisitions. The board expects to raise the dividend above inflation, more in line with earnings growth, thereby maintaining dividend cover at around two times earnings in the long term.

Pensions

Pearson operates a variety of pension plans. Our UK Group plan has by far the largest defined benefit section. We have some smaller defined benefit sections in the US and Canada but, outside the UK, most of our companies operate defined contribution plans.

The income statement expense for defined benefit plans is determined using annually derived assumptions as to discount rates, investment returns and salary inflation, based on prevailing conditions at the start of the year. The assumptions for 2010 are disclosed in note 25 to our accounts, along with the year-end surpluses and deficits in our defined benefit plans.

The charge to profit in respect of worldwide pensions and post-retirement benefits for continuing operations amounted to £102m in 2010 (2009: £90m) of which a charge of £90m (2009: £78m) was reported in operating profit and the net finance cost of £12m (2009: £12m) was reported against net finance costs.

The overall deficit on the UK Group plan of £189m at the end of 2009 has become a deficit of £5m at 31 December 2010. This decrease is principally due to an increased level of contributions in the year together with improved asset performance. In total our worldwide deficit in respect of pensions and post retirement benefits fell from a deficit of £339m in 2009 to a deficit of £148m at the end of 2010.

Acquisitions

On 17 June 2010 the Group acquired Melorio plc, one of the UK's leading vocational training groups for £98m.

On 22 July 2010 the Group announced that it had entered into an agreement to purchase the learning systems business of Sistema Educacional Brasileiro (SEB) one of Brazil's leading education companies for approximately $517m. The agreement provided for the acquisition of the business in two tranches – the first of these tranches representing 69% of the business was acquired on 1 September 2010 for $357m and the remaining tranche is expected to be acquired in the first half of 2011.

Other financial information continued

On 19 August 2010 the Group completed the acquisition of Wall Street Institute Education S.a.r.l. (WSI) for $101m. WSI provides spoken English training for adults through a combination of web-based content, classroom instruction and digital and printed materials.

The acquisition of America's Choice, a provider of educational solutions for states and school districts in the US, was completed on 7 September 2010 for $101m.

The Group also completed the acquisition of Medley Global Advisors LLC and various other smaller acquisitions in the year. Although the Group has announced the acquisition of CTI Education Group and the increased stake in TutorVista, these transactions did not complete until 2011.

Net cash consideration for all acquisitions made in the year ended 31 December 2010 was £535m and provisional goodwill recognised was £288m.

In total, acquisitions completed in the year contributed an additional £84m of sales and £6m of operating profit.

Return on invested capital (ROIC)

Our ROIC is calculated as total adjusted operating profit less cash tax, expressed as a percentage of average gross invested capital. ROIC increased by 1.4 percentage points from 8.9% in 2009 to 10.3% in 2010. Improved profit performance and a reduction in working capital were the main drivers behind the increase. Although cash tax rates were low in 2010 we expect an increase in tax payments in 2011 as US tax losses are now fully utilised.

Capital expenditure

Net capital expenditure in the year on property, plant equipment and software amounted to £144m. The analysis of capital expenditure and details of capital commitments are shown in notes 10, 11 and 33 of the financial statements.

Related party transactions

Transactions with related parties are shown in note 34 of the financial statements.

Post balance sheet events

On 22 November 2010, the Group announced the proposed acquisition of a 75% stake in CTI Education Group, a leading South African education company for £31m. As at the end of December 2010 this acquisition had not been completed but is expected to complete in the first half of 2011.

On 18 January 2011, the Group announced that it had agreed to increase its shareholding in TutorVista, the Bangalore based tutoring services company, to a controlling 76% stake for a consideration of $127m.

On 7 March 2011, the Group and Education Development International plc (EDI) announced that they had reached agreement on the terms of a recommended cash offer to be made by Pearson for the entire issued share capital of EDI. The offer values EDI at approximately £112.7m. EDI is a leading provider of education and training qualifications and assessment services, with a strong reputation for the use of information technology to administer learning programmes and deliver on-screen assessments.

Supplier payment policy

Operating companies are responsible for agreeing the terms and conditions under which business transactions with their suppliers are conducted. These supplier payment terms vary by operating company reflecting the different industries and countries in which they operate. It is company policy that suppliers are aware of such terms of payment and that payments to them are made in accordance with these, provided that the supplier is also complying with all the relevant terms and conditions. Group trade creditors at 31 December 2010 were equivalent to approximately 30 days of purchases during the year ended on that date. The company does not have any significant trade creditors and therefore is unable to disclose average supplier payment terms.

Principal risks and uncertainties

Our principal risks and uncertainties are outlined below. These are the most significant risks that may adversely affect our business strategy, financial position or future performance. The risk assessment process evaluates the probability of the risk materialising and the financial or strategic impact of the risk. Those risks which have a strong probability and significant impact on strategy, reputation or operations or a financial impact greater than £40 million are identified as principal risks. The risk assessment and reporting criteria are designed to provide the board with a consistent, Group-wide perspective of the key risks. The reports to the board, which are submitted every six months, include an assessment of the probability and impact of risks materialising, as well as risk mitigation initiatives and their effectiveness.

We conduct regular risk reviews to identify risk factors which may affect our business and financial performance and to assist management in prioritising their response to those risks. Our Group internal audit function facilitates risk reviews with each business, shared service operations and corporate functions, identifying measures and controls to mitigate these risks. These reviews are designed so that the different businesses are able to tailor and adapt their risk management processes to suit their specific circumstances. Management is responsible for considering and executing the appropriate action to mitigate these risks whenever possible. It is not possible to identify every risk that could affect our businesses, and the actions taken to mitigate the risks described below cannot provide absolute assurance that a risk will not materialise and/or adversely affect our business or financial performance.

In addition to the principal risks described here, further information on other risks and how they are addressed can be found on pages 172 and 173.

Principal risks and uncertainties continued

Principal risks	Mitigating factors
Our education, business information and book publishing businesses will be impacted by the rate of and state of technological change, including the digital evolution and other disruptive technologies.	We are transforming our products and services for the digital environment along with managing our print inventories. Our content is being adapted to new technologies across our businesses and is priced to drive demand. We develop new distribution channels by adapting our product offering and investing in new formats. We are actively monitoring contraction in the consumer book market to minimise the downturn of bankruptcy.
Investment returns outside our traditional core US and UK markets may be lower than anticipated.	We draw on our experience of developing businesses outside our core markets and our existing international infrastructure to manage specific country risks. We have strengthened our financial control and managerial resources in these markets to manage expansion. The diversification of our international portfolio, and relative size of 'emerging markets' in relation to the Group, further minimises the effect any one territory could have on the overall Group results.
Our US educational solutions and assessment businesses may be adversely affected by changes in state and local educational funding resulting from either general economic conditions, changes in government educational funding, programs, policy decisions, legislation at both at the federal and state level and/or changes in the state procurement processes.	We actively monitor changes through participation in advisory boards and representation on standard setting committees. Our customer relationship teams have detailed knowledge of each state market. We are investing in new and innovative ways to expand and combine our product and services to provide a superior customer offering when compared to our competitors, thereby reducing our reliance on any particular funding stream in the US market. We work through our own government relations team and our industry trade associations including the Association of American Publishers. We are also monitoring municipal funding and the impact on our education receivables.

Principal risks	Mitigating factors
A control breakdown or service failure in our school assessment businesses could result in financial loss and reputational damage.	We seek to minimise the risk of a breakdown in our student marking with the use of robust quality assurance procedures and controls and oversight of contract performance, combined with our investment in technology, project management and skills development of our people.
Our reported earnings and cash flows may be adversely affected by changes in our pension costs and funding requirements.	We review our funding arrangements every three years and will take steps to ensure pension funding plans are sufficient to meet future liabilities without unduly affecting the development of the company.
Our intellectual property and proprietary rights may not be adequately protected under current laws in some jurisdictions and that may adversely affect our results and our ability to grow.	We seek to mitigate this type of risk through general vigilance, co-operation with other publishers and trade associations, advances in technology, as well as recourse to law as necessary. Data rights management standards and monitoring programmes have been developed. We have established a piracy task force to identify weaknesses and remediate breaches. We monitor activities and regulations in each market and take legal action where necessary.
A major data privacy breach may cause reputational damage to our brands and financial loss.	Through our global security office under the direction of our Chief Security Officer, we have established various data privacy and security programmes. We constantly test and re-evaluate our data security procedures and controls across all our businesses with the aim of ensuring personal data is secured and we comply with relevant legislation and contractual requirements. We regularly monitor regulation changes to assess impact on existing processes and programmes.
Operational disruption to our business caused by our third party providers, a major disaster and/or external threats could restrict our ability to supply products and services to our customers.	We have developed business continuity arrangements, including IT disaster recovery plans and back-up delivery systems, to minimise any business disruption in the event of a major disaster. The governance structure, overseen by a global coordinator, provides the capability to centrally monitor all related activities. Full contingency plans have been completed for all high and medium risk locations and are updated on a regular basis. Insurance coverage may minimise any losses in certain circumstances.